RICHARD RUSSELL'S DOW THEORY LETTERS INCORPORATED

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October 31, 1984 LETTER 899

Oct. 19, DJIA 1225.93; PTI 1625; A-D Ratio –19.71
Oct. 26, DJIA 1204.94; PTI 1609; A-D Ratio –20.25

THE PICTURE: Nothing is more important to investors than a knowledge of the direction of the primary trend. The primary trend is the fortune builder, the great force that ultimately turns 85% of your purchases to profits if you are in a bull market – or 85% of your stockholdings to losses if you are in a bear market.

Personally, in my own security operations I devote about 60% of my studies to the primary trend, perhaps 30% of my studies to the secondary trend, and the remaining 10% to the daily or minor trend.

Periodically I have listed six criteria with which I attempt ***to gauge the direction of the primary trend.*** I want to review those six again now.

(1) The Dow Theory indicates that the primary trend is bullish. Both the Industrial and Transportation Averages (see chart below) are now well above their May 2 secondary highs, a bullish sign. More recently, however (and this could be very important) the D-J Industrial Average failed to confirm the new recovery high in the Transports. A bullish upside confirmation would require Industrials to better the August 21 peak of 1239.73. A persistent refusal at this point to better 1239.73 – could spell trouble.

(2) My PTI (see page 2 chart) has been pushing (rather sluggishly) higher, but the DJIA has not confirmed the strength in the PTI. In the past, this has been a forerunner of trouble, so let's hope the Industrials do confirm (by bettering the 1239.73 high).

(3) The ***Bank Credit Analyst's*** debit/loan ratio has been caving in. This has always been a harbinger of falling corporate profits (and profits are indeed falling). I rate the debit/loan ratio bearish.

(4) The ***Trendex*** Long Term Probability Pattern for the NYSE Composite turned bearish on February 1, 1984. It is still bearish.

(5) A bright spot is Lowry's Buying Power/Selling Pressure study. This study turned bullish on October 15.

(6) Ned Davis's "Big Mo" longer-term market indicator is slightly bearish. This is a longer term negative for the market.

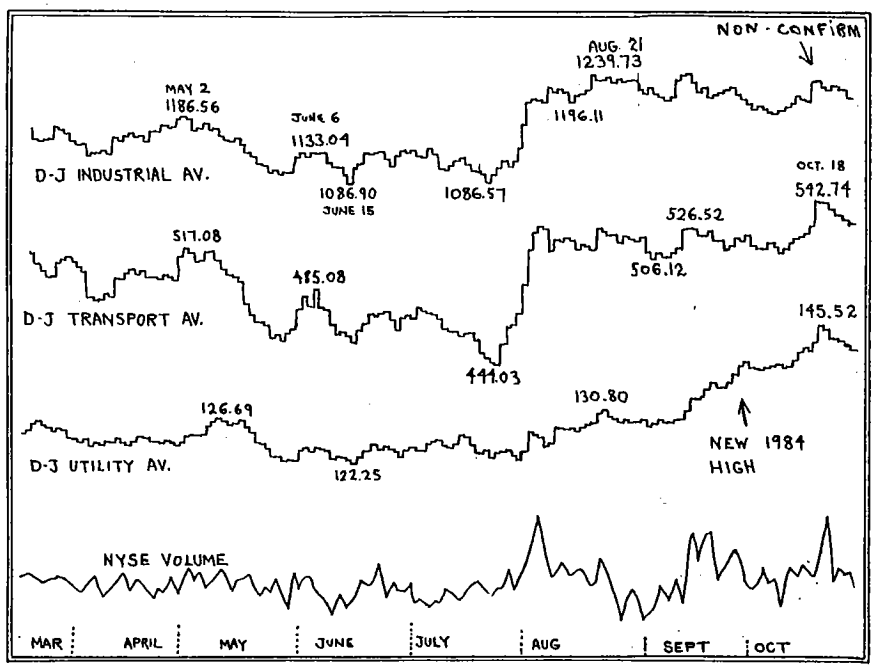
I feel that this is the most important Letter that I have written in some time. The reason is that the market is at the most critical juncture it has been in many months.

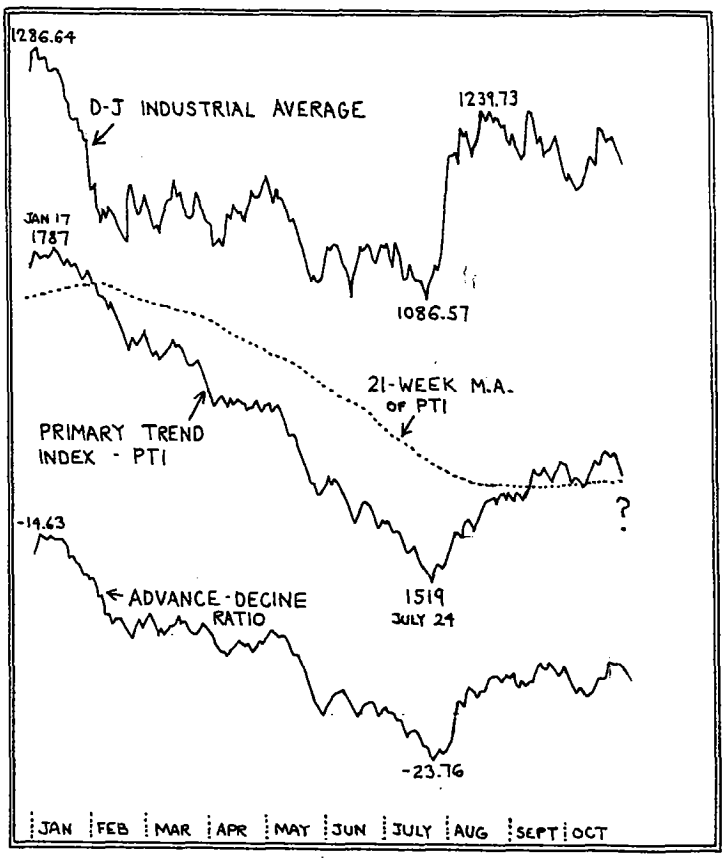
Why do I say that? The reason is that corporate profits are now visibly contracting. How long the contraction will last or how severe the contraction will be no one knows. But it will be extremely IMPORTANT to see HOW the market reacts to the current business news. If the market holds up in the face of the many downward revisions in the third quarter earnings statements – then all well and good. But if the market turns down here, if the PTI drops below its 21-week moving average, if the Dow breaks below its 30-week moving average at roughly 1175, then I am going to become very concerned. So I believe that we are at a critical juncture. But I am willing to let the market tell the story.

Question: What about money rates and the Fed action at this juncture?

Answer: The Fed hasn't been immune to the coming election or the signs of an economic slowdown (dare we call it recession?). Thus, the Fed has had a double-barreled reason for easing up here. And, of course, the stock market appreciates it. Thus, we now have a struggle between lower interest rates (bullish) and lower corporate earnings (bearish). The BIG question (which the stock market will answer in due time): is the earnings fall-off the prelude to a slowdown – or a severe recession? We should know soon.

Question: You've been talking disinflation or actual deflation for quite a while. What are your latest thoughts on deflation?





Answer: If disinflation can progress ***gradually***, all may be well. But if deflation comes in strongly, that's a different story, and it could be a very bearish story. For instance, IF oil prices collapse many Arab nations will dump their US T-bonds and bills in order to raise money. That would send interest rates through the roof. Again, if oil prices plunge then many bank loans (based on high priced oil as collateral) will be in great jeopardy. And there you have two examples of what could happen if just the price structure of oil gets out of hand on the downside. So gradual disinflation is one thing, but rampant deflation is another. Let's hope we don't see the latter.

Question: Russell, what do you see for the economy in the months ahead?

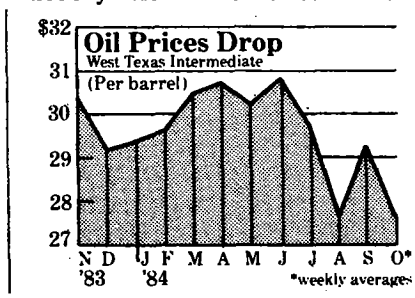
Answer: I honestly don't know. But as I said before, a bearish turn in the market here would tell me that the odds for a recession in 1985 are high, very high.

Question: What would happen to interest rates if a recession hits?

Answer: This is the biggest question of the year. Many believe that a severe recession would bring interest rates way down. I'm not at all convinced. If a recession hits, today's $175 billion federal deficit is going to climb way over $200 billion (probably over $250 billion!). If that happens, if the bond market starts looking at a quarter trillion dollar deficit, then I think interest rates could go through the roof again, regardless of what the Fed tries to do. In that case, you could see all kinds of financial and bank troubles and a huge widening of the spread between highest grade credit instruments and lower grade instruments.

Question: What about oil, bonds and interest rates?

Answer: No need to guess about either of these. I have been showing charts of oil and bonds all year, and this is probably the time to do it again. Heating oil has now broken down to new lows, and the price structure of world oil is sagging. The reason is fundamental – there's a lot more supply than demand. Thus, the pressure is on OPEC, and already the great cartel shows signs of coming apart at the seams. Remember, many OPEC members have taken on huge projects and expenses, and they HAVE TO sell oil. The result: nobody knows who will cut the oil price next.



The effect of lower oil prices is still tantamount to a huge tax cut across the face of the earth. But it's still deflationary, and it makes everything feel cheaper. Since the price of black gold (i.e. oil) is one of the real bellwethers of world trade, when oil prices decline people think deflation.

Bonds, already in a well-defined bull trend before the most recent oil price cuts, exploded on the news of further cuts. The roaring bond market produced lower interest rates, and the lower interest rates spurred the stock market.

Question: You have been talking about the Utility Average for quite some time. I note the recent outstanding strength in Utilities. What does it mean?

Answer: On October 16 the D-J Utility Average rose to its highest level since 1966. This can hardly be termed a bearish event. No, it is basically a plus for the market. I have run this point & figure chart a number of times over the last year, each time drawing attention to the huge head-and-shoulders bottom, and each time stating that the potential for bullish action here was very great.

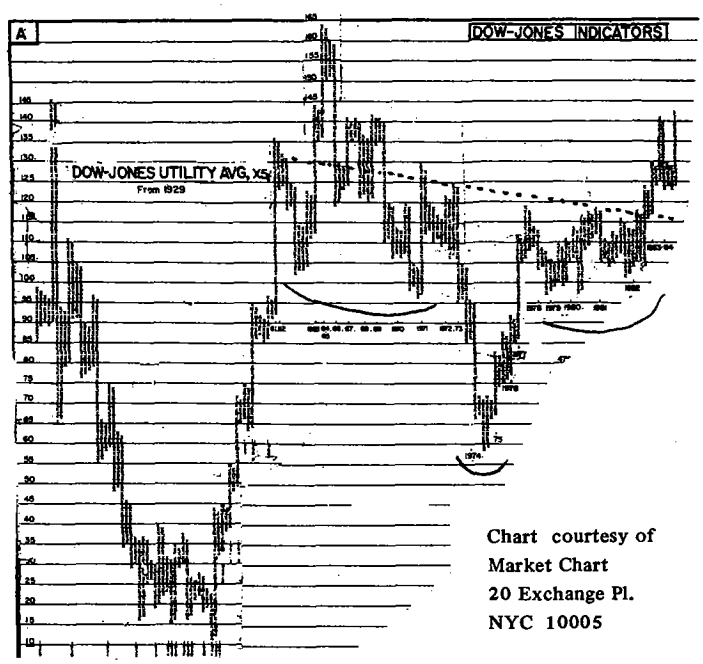


Chart courtesy of
Market Chart
20 Exchange Pl.
NYC 10005

I include the chart again with this Letter, with the statement (again) that the upside potential for the Utility Average is impressive. The Utility Average is the only major Average that has failed to better its old 1965-66 bull market high, and a move above the 1965 high for the D-J Utility Average would entail a rise above 163.32.

As I have stated before, a joint rise by utilities and bonds exerts a very powerfull influence on the market. Such a rise has been occurring over the last few months. When bonds and utilities are locked in gear on the upside (or the downside) the rest of the market almost always follows. However, at this point bonds and utilities are ***ready to correct.***

Question: Russell, what about the Value Line chart, please go over that one again.

Answer: I have shown the point & figure chart of the Value Line because (1) the Value Line is a very broad stock index, and it is inconceivable that the Value Line Composite could rise or fall without taking the entire market with it, and (2) because the Value Line has been in a major basing pattern. That pattern is a head-and-shoulders bottom, much like the pattern of the Utility Average.

The Value Line chart particularly interests me because of all the bottoming patterns I have worked with, the one that I have found to be most reliable is the head-and-shoulders bottom, the kind that the Value Line Composite has now formed.

Now obviously, no pattern, index or technical study is infallible. In other words, any study can abort. But I would say that three out of four head-and-shoulders bottoming patterns work out. For that reason, I believe that this market has the capability of fooling skeptics, in that the Value Line pattern is capable of sending the stock market substantially higher – in due time.

Question: Russell, in your experience, what is the safest method of investing?

Answer: I've stated this many times, but I'll say it again. The safest method of investing is to ***compound very safe securities.*** I don't care whether those securities are industrial stocks, utilities, municipal bonds or T-bills. The two major criteria for correct and profitable compounding are (1) the security must be SAFE. There is no sense at all in compounding a security that is going to go bankrupt. (2) Attractive yield. The higher the yield, the better the rate of compound return.

I should add a third factor, and that is the tax consideration. If you are talking about a tax deferred account such as a pension plan or an IRA then you should probably go for the highest safe yield, such as a T-note or T-bond. But if you are compounding in your own account it may be that municipal bonds (if you are in a high tax bracket) present the best area for compounding yourself to riches.

As I've written so many times, compounding entails patience and discipline, two qualities that most people lack. Compounding entails sticking to a plan (discipline), and for that reason the vast majority of investors never get rich via the only SURE method – compounding.

Question: Russell, what do you make of all the warnings that we hear from leading economists regarding "a severe recession in 1985"?

Answer: I like widely advertised predictions. I like them because a widely advertised prediction gives the market time to absorb the full impact of the prediction and to discount it. It is the REACTION of the market to the prediction that interests me, not the prediction.

The following is in no way a reflection on the predictors, but I am going to cite a few extraordinary examples of widely advertised predictions along with the results.

(1) Back in 1974 the famous E. George Schaefer predicted that gold would take off on a massive rise into the stratosphere. Gold and gold shares did just the opposite, Schaefer ended up committing suicide and many gold share holders were wiped out. Later (a few years later) gold did explode, but Schaefer's predictions were right too soon.

(2) A few years ago the Aden sisters (and they are very smart) predicted a major bull market rise in gold which would take the metal back near the old highs by 1984 or 1985. The Adens received a tremendous amount of publicity (I doubt if they even wanted the publicity), but their predictions did not materialize. Gold followers are still waiting for the explosion.

(3) In one of the most widely-publicized "signals" in history, Joe Granville (in January 1981) advised his followers to "sell everything." The market broke for a few days, then rallied, then

The Recession Is Already Upon Us

By S. JAY LEVY and DAVID A. LEVY.

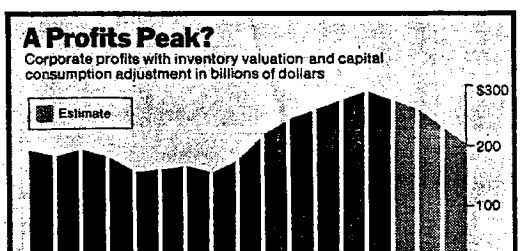
THE next recession is already here.

Early in the year, when we warned that it might hit, we encountered an understandable degree of puzzlement and skepticism. But now the evidence of a recession spans three consecutive months of predominantly bad economic news.

The volume of housing construction, a bellwether of the economy, peaked in the first half and has been sliding rapidly. Business reduced its orders for new capital equipment three months in a row, and has scaled down its plans for investment in new plant and equipment during the rest of 1984.

Retail sales declined during the summer. The spurt of back-to-school business was late and short-lived. Inventories, already excessive for many companies, have been rising faster than sales, and efforts are underway to reduce stocks. Industrial production barely increased in August. Employment is decelerating, claims for unemployment benefits are rising and help-wanted ad volume is falling.

Why has the recovery ended? In our profit-driven economy, recessions occur when business profits fall — companies cannot sell as much as they expected to sell at the prices they expected to receive. Weaker business conditions cause businesses



interest rates gave the recent recovery an early impetus. Housing starts reached a peak of 2.25 million units — on an annualized basis — last February. They have fallen to 1.5 million and the reports of lending institutions on the recent dearth of home sales and mortgage applications suggest that the decline in residential construction has a way to go.

Even more essential to the strength of the over-all economy is business investment in non-residential buildings and equipment. During the past year, the real growth of capital outlays set records and was a major propellant of the recovery. Business capital expenditures usually lag the business [illegible] they are already showing cut stocks. The low rate of inflation — indeed, prices for many industrial materials are declining — is encouraging purchasers to carry smaller inventories. That is a marked change from the 1970's, when companies often bought ahead to beat price increases.

PROFITS also suffer when consumers refrain from spending. Consumers spent freely in 1983; their saving rate was at a 30-year low. In 1984 the saving rate has been moving up and the receipts of retailers and other consumer product firms have suffered accordingly. In the first half of this year consume[illegible] were still borrowing [illegible] skimming the cream off milk takes away a great portion of the butter fat but leaves most of the total liquid, a trade deficit removes a large share of profits while affecting only a small share of sales.

Here is an illustration of why. Suppose that American consumers have $110 billion a month to spend and that American business has goods for sale that had cost it $100 billion to bring to market. If consumers spend all of their $110 billion on American goods, the nation's enterprises will have a $10 billion profit. But say that consumers spend $10 billion for foreign goods and only $100 billion on domestic products. American businesses' pre-tax profits would be reduced by as much as $6 billion.

The trade deficit has another insidious effect on American prosperity. As domestic industry loses sales to foreign enterprises, its idle capacity increases and its receipts decline. It has less need for and less ability to pay for inventories, new plant or equipment.

Thus, a number of forces are combining to push profits lower, a process that will snowball as business begins to retrench. Indeed, the drop in profits will likely be the most severe of any postwar recession.

This recession would be bad news no matter when it occurred. Yet in salient ways its timing is especially unfortunate. It is the third contraction in only five years, and it [illegible] economy

sank further. But Granville was ridiculed because by March of '81 nothing too bad had occurred, and, in fact, the market had recovered. But a new decline continued into August of '82. However, nobody remembered that Granville had made a good long-term call. They only remembered that nothing drastic had occured three months after the Granville call.

(4) In early 1984 Henry Kaufman and Al Wojnilower predicted that bond rates would hit new highs by the end of the year. Instead, bond rates started easing and instead of going to 15% or higher as predicted, bond rates are now around 12%.

(5) A current widely-advertised economic forecast particularly interests me. It was made by the highly respected David and S.J. Levy in their "Industry Forecasts." The Levys went public with this forecast in the Sunday *New York Times* (Oct. 14), and I include a section of that article (page 3). Could the Levys be correct? Of course they could. But I am somewhat comforted by the fact that the bearish Levy forecast has received such wide publicity. Drastic stock market movements and drastic economic events are usually not advertised in advance. They tend to come "out of the blue." So the more publicity "the coming severe recession" receives, the better I like it, because at least I'll get a chance to see HOW THE MARKET REACTS TO IT.

But I don't want to be a wise guy. The Levys are smart as a whip, and I take what they say and what the Bank Credit Analyst's debit/loan ratio says very seriously. If the bearish forecast even BEGINS to be proven right, I'll be the first fellow to get with it. So as I say, the market (as a barometer of coming events) is at a very critical juncture right now.

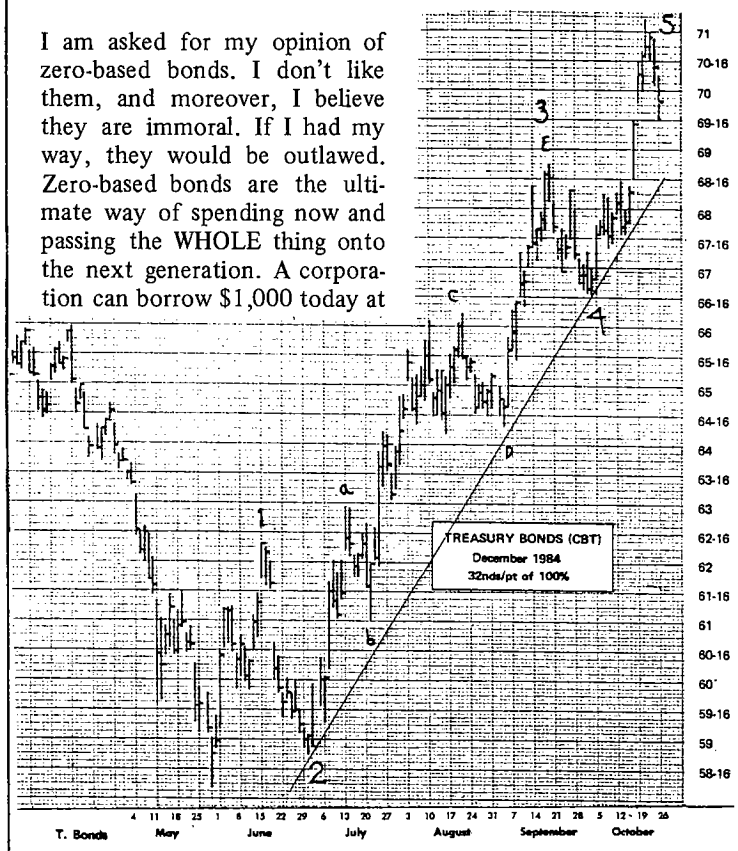
(6) Four well known and respected investment advisors are now warning of a possible crash during what remains of 1984 or during 1985. They are Joe Granville, C. V. Myers, Donald Hoppe and Julian Snyder. Almost everyone in this industry has heard of, or knows about, their dire predictions. Could they be right? Sure they could. But I remain a bit skeptical. I'm skeptical because (a) a crash is such a rare event, and the odds on correctly predicting such a once-in-a-lifetime event are slim. (b) Crashes, like economic depressions, usually come when least expected. But again, I don't want to be a wise guy. Even prior to 1929, a few people were prescient enough to warn of major danger. So maybe Granville, Myers, Hoppe and Snyder will be the heroes of this era. But I still depend on *market evidence* for my facts, inferences and decisions.

INVESTMENT POSITION: My position is simple enough. The bull is in this box, and he will remain there as long as the PTI remains bullish. So with the bull in the box, we sit with our stocks.

The investment I've liked BEST (and I've repeated this in Letter after Letter) is the longer-term bonds. Back in June (when I recommended buying the bonds) nobody wanted them – even though rates on Treasuries were juicy. Now everybody wants bonds, and of course, the T-bonds are up about 17%. This daily chart (courtesy of Dunn & Hargitt) shows the big bond move, and last week we saw some panic buying (which created the upside gaps).

What to do with the bonds now? Simple, hold them as long as they fluctuate ABOVE the rising trendline. If T-bond futures (December) break below 68½, take the profits. If they stay above 68½, stay with them and collect fat interest payments. As you can see on the chart, I get an Elliott five-count on the bonds with panic buying in leg 5. Thus, a correction is in order – now.

I am asked for my opinion of zero-based bonds. I don't like them, and moreover, I believe they are immoral. If I had my way, they would be outlawed. Zero-based bonds are the ultimate way of spending now and passing the WHOLE thing onto the next generation. A corporation can borrow $1,000 today at



13%, ***pay nothing*** for the next 20 years (it could even be close to insolvency for most of that time), and then it has to come up with the whole thing, $13,300 in 20 years. Talk about immorality, talk about shifting the burden to our kids, this is it. I wouldn't buy zero-based bonds, I wouldn't sell them to anyone, and I wouldn't recommend them. I think the whole idea is a can of worms.

TOUGHING IT: I've been through this before, but I'm writing about it for the interest of my subscribers and as an aid to younger members of the investment advisory fraternity. For some time I've felt that the financial and advisory community was overcrowded – saturated. From here on in, I believe we are going to see a major weeding out of the marginals – and maybe some of the biggies.

What's the evidence? Here's some: (1) Financial News Network in LA has just announced that they are shutting down most of their operations on the West Coast. Almost all personnel have been fired. (2) Five advisory services (including Hulbert and Dessauer) in fullpage ads are offering subscriptions for $19 to $24 annually whereas their regular price runs $135 to $225. For whatever reason they are doing this, it's not a good sign. (3) The LA Times (Sept. 8) includes an article about Dow Jones entitled "Earnings Drop May Mark End of Era for Dow Jones." Circulation of the WSJ and the earnings for DJ have declined. (4) Brokerage house stocks have caved in. Merrill Lynch hit a high over 56 in 1983. The stock has already lost half its peak value, is now selling for 27.

Conclusion: The bull market in financial news may have topped out .

NOTES & QUOTES: The Presidential debates, to my mind, were mostly nonsense. But they gave the nation a chance to look

at the two candidates. Actually, I thought Reagan was crazy to even debate with Mondale. A winner doesn't have to prove himself – he's already there. I doubt if the debates succeeded in switching many votes. I thought Reagan looked good in the second debate, and Americans obviously love the Irish twinkle in his eyes. Mondale has eyes that look like soft boiled eggs, and he comes across as intelligent but tense and somehow rather unpleasant.

Most startling fact to come out of the political picture – the under 25 group is heavily for Reagan, particularly at the college level. Why? Answer seems to be that "Reagan is strong, he has convictions." My own feeling is that the public (and I'm including union people, blue collar workers, middle class, everybody) knows that the old Democratic Party answers don't work any more. It's a new world, a new Russian, a new peak in Federal deficits, a new ferocity in competition for US business. The public senses that the Republicans have the correct philosophy, if only they had the guts to implement that philosophy.

The welfare state is now against the wall, and the wall is crumbling. Americans know it; they see what's happening in Europe. And they feel that the Democrats would send this country right into the European welfare miasma. In their hearts, Americans know that 2 plus 2 equals 4. They just have been hesitant about facing it.

The paradox: Mull this over. We elect the politicians. The politicians are spending the nation into bankruptcy. We (the people who elect the politicians) are now moving towards a Constitutional Convention which would stop our own politicians from running an insanely unbalanced budget. BUT, if we get a balanced budget that would entail both higher taxes and massive cuts in government spending. At which point, the people would start screaming for more spending. So it seems to me that the situation is out-of-control. The debt and deficit situation has taken on a life of its own.

I have to laugh at the Democratic press's wild efforts to discredit Reagan. The effort has almost reached hysterical proportions in the New York Times, the LA Times and the Washington Post. Reagan is revealed as "too old," as man "always asleep at his desk, "a man unaware of what's happening around him, a man who mumbles, bungles questions, a man who should be in a geriatric home rather than in the White House." Evidently, the Democrats have decided that there's more return in attacking Reagan and Bush than there is in touting Mondale and Ferraro. At any rate, that's the way the campaign is going.

Probably the most telling item on the coming election is right here in this squib. This is money talking:

> ***British Bookmakers Close Betting on Reagan at 1-7***
>
> LONDON (UPI) – Britain's largest bookmakers, Ladbroke's, stopped taking bets for President Reagan to win a second term because the odds were so low it "just wasn't worth it anymore" for people to bet on him.
>
> The odds on Mr. Reagan winning closed at 1-7.

* *

Statistics: According to a Newsweek poll, 42% of Americans couldn't pay a bill for $1,000 if it came up.

A surprising 52% of college students are now women. Between 1972 and 1982 the US college population rose 3 million. And 80% of the increase was women.

* *

What do you get when you fight the primary trend? Losses! The story of the Hunt brothers and silver is unbelievable. It now turns out that the Hunts still hold 59 million ounces of silver. It is estimated that the Hunts may have accumulated losses of around $2 billion on their silver, and they have still not sold! You think that billionaires always know what they are doing? Forget it! To me the amazing thing is that the Hunts can sustain that kind of paper loss and still be solvent. At any rate, here are a few paragraphs from the Oct. 18 WSJ:

> They appear to be reluctant to fulfill their promise to their lenders to dispose of the silver "in an orderly manner." They also have paid dearly for holding the silver. Besides an initial loss of about $1 billion, silver traders and government officials estimate they have paid an additional $600 million in debt interest and have another $400 million in paper losses.
>
> Sources close to the brothers said "there has been no change" in their 59-million-ounce holdings. Both Nelson Bunker Hunt and W. Herbert Hunt, these sources said, are determined to hold on until silver prices recover and the two can recoup their losses. Nelson Bunker Hunt did much the same thing in the mid-1970s when he held about 40 million ounces of silver for several years after a price decline.
>
> The two Hunts, and to a lesser extent Lamar Hunt, had a loss of close to $1 billion in early 1980 when the silver market crashed to $10 an ounce from a midday high of $50 an ounce in a few weeks. The Hunts helped force silver prices to record levels by taking delivery of huge amounts of silver and buying futures contracts for much more. But the price broke, at least partly because of emergency trading restrictions imposed by two U.S. commodity exchanges, whose directors allegedly included traders hurt by the price explosion.

* *

Trying to horn in on the NFL, the new USFL football league has lost near $100 million so far. So what's next? Naturally, the USLF is suing the NFL for $1.3 billion, and it will be a race to see whether the USFL goes under before the case comes to trial. In the meantime, TV popularity for pro football is caving in. The public has been turned off by lawsuits, strikes, college games all over the tube, USFL games, NFL games and on and on. Last week the Pittsburg Maulers (with a loss of $9 million) threw in the sponge. They're disbanding.

Even Donald Trump, the hero of Gotham, is wondering why he jumped into football. Here's his latest word on the world of professional sports:

> **Rumors that he would buy the San Francisco Giants were denied by Donald Trump, owner of the New Jersey Generals of the USFL.**
>
> **"I am not interested in buying the San Francisco Giants," Trump said. "Sports is a lousy business—the worst."**

* *

Justice: Ever wonder who is responsible for all those billions in lousy loans put out by the banks? Well, evidently the banks are

beginning to wonder, too. Chase Manhattan is suing six former loan officers for $175 million, charging they ignored "obvious risks" when they bought energy loans from Penn Square Bank. The whole banking world is watching and the key word is negligence. If Chase wins, the fireworks could start – because there is a mountain of bad loans out there, no, more like a mountain range of loans!

* *

Horror Show: This is the wrong spot for this comment, but I just got the figures, and I had to put them in somewhere. The latest figures show that the US Treasury took in $666.4 billion in revenues during 1984. During the same period they paid out $153.8 billion in interest! Ye gads, that means that interest costs are now 23% of all the receipts the US government took in! We are BEING EATEN ALIVE BY DEFICITS AND DEBTS. And take it from me, this whole trend of deficits and compounding the debt will lead to disaster. On the basis of what I see, a recession in 1985 would send the US Treasury into the damnedest mess you've seen. I am telling you, my subscribers, that these guys in Washington don't understand what's happening. On the basis of fundamentals, I'm beginning to think that all of us should start building CASH. The word for 1985 could well be – cash, cash, cash!

* *

Books: I still receive lots of letters from subscribers wanting to know more about the Dow Theory. Back a few years ago I wrote a series of articles for Barron's, and later I collected the series in a book. The book has been reprinted by Fraser Publishing, Box 494, Burlington, VT 05402. I include this paragraph from the Fraser catalogue:

> **THE DOW THEORY TODAY** RICHARD RUSSELL
>
> A collection of twelve articles written for Barron's between 1958 and 1960, this book was first published in 1961 and has since been long out-of-print. The time span of the articles was a particularly difficult one for investors and traders and for the market analyst who must put his opinions on record. Some of the articles pertain to general Dow theory or to market history as interpreted under Dow's Theory. Other articles deal with the price movements on the dates specified. All in all, this is an important book for both market students and historians and should be part of every library. 119 pages. Flexible cover, **061-I $7.00.**

* *

Have you heard this one? A survivalist was talking to his friend. "Buddy, ah've been diggin' in. I spent $12,000 on a cement bunker, ah put $3,000 worth 'a dried food in the basement. I bought an Uzi and a Remington pumpgun for $2,000. Ah got $5,000 worth of half ounce Krugerrands buried in plastic tubes under the vegatable garden, an ah got bullet-proof vests for the whole family at $400 a piece. Ah mean, man, if the end of the world doesn't come soon – ah'm RUINED!"

* *

What's happening to the "Star Wars" defense system? The US is definitely going into it! Last week I spoke to Mel Lippman of US Organization Chart Service here in La Jolla (he is a publisher of military and industrial information), and he told me that in February, 1985 the new Strategic Defense Department will be accepting bids on 10-12 totally new projects from 250 military bidders. The projects will be for systems to stop ballistic missiles from coming in from outer space. The systems will be expected to intercept incoming missiles from every stage – from boost to post-boost to on-course. These will be all new technologies.

Some hint of what's going on can be seen in the new Defense Dept. military budget. For 1985 the DD is asking for $333.7 billion, 13.9% above this year's budget.

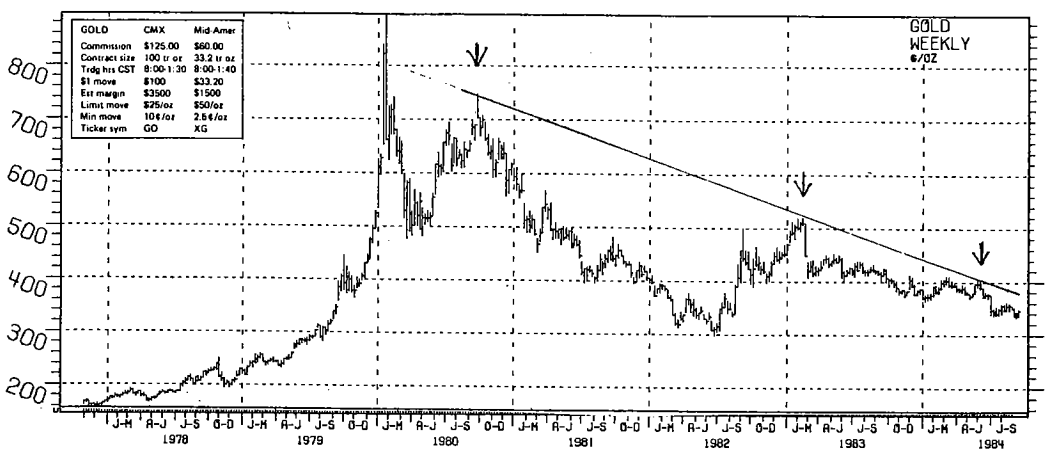
GOLD: Picture this: a stock sold four years ago for as high as 85. But by late 1984 the stock has fallen to 34. The stock tends to move up on inflation and down on deflation. It pays no dividends but is an asset play.The stock has been in a bear trend ever since 1980, and at present (giving it every benefit of the doubt) its trend is simply unclear. Would you buy it? Probably not. I know I wouldn't.

Now substitute gold for the stock, and you've got the picture. But wait a minute, gold has a mystique, gold is real money, gold has a following, there are people out there who LOVE gold. And I'm one of them. And that's why I still have about 25 one-ounce Maple Leafs. But back in 1980 (when I was bullish on gold) I had over 1,000. And that's the way it goes. Gold is like a pretty woman. You can love her, but you don't have to own her. At least not when the trend is against you.

With the trend down for gold ever since 1980, it's amazing that there are still so many ads and so many analysts urging us to buy gold. You'd think a four-year bear trend would have discouraged them. It hasn't. The slightest rise in the bullion causes the gold shares to "pop." So my guess is that when gold really is a buy, it will be thoroughly discredited, and today's believers will have been ground into history.

Friends continue to tell me that "all this borrowing" is going to end up in an inflationary boom. I tell them that it's more likely to end up in an interest rate explosion, a financial crisis, and deflation. But, of course, I'm just guessing – let history be the judge.

LATE NOTES: The non-confirmation on the part of the D-J Industrials is beginning to look a bit ominous. Downside danger points to watch are 1175.13 (Industrials) and 506.12 (Transports). A joint breaking of those two levels would constitute a sell signal. Any weakness early this week will take the PTI below its 21-week Moving Average. This market could easily turn nasty.



NEXT MAILING: Nov. 15